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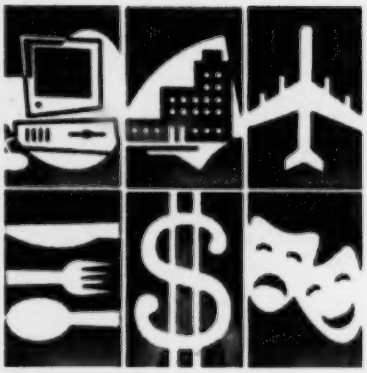
Changing Market Trends: How Technology and Global Conditions Affect the Canadian Travel Industry



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Changing Market Trends: How Technology and Global Conditions Affect the Canadian Travel Industry

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Introduction:

This article gives an overview of the Canadian travel distribution[1] and travel accommodation sectors[2]. Travel distribution consists primarily of two key players: retailers (travel agencies) and packagers (tour operators). Travel accommodation refers mainly to the hotel and motel industry in Canada. Findings are based on a panel of surveyed establishments within these travel industries[3]. Results come from the *Annual Survey of Travel Arrangement Services*, and the *Annual Survey of Traveller Accommodation.*

The first part of this article looks at the challenges these industries face in a rapidly changing and increasingly technological environment. The second part examines how global conditions adversely affected the travel industries in 2003.

Part 1: How technology has affected the travel industries

Travellers' use of the Internet has grown

One of the most important recent technology advances, the Internet, may be viewed as an opportunity by some travel service providers while appearing threatening to others. The Internet's increased popularity has had a major impact on the travel industry over a relatively short period of time. In the beginning, travel suppliers went on-line to provide information. Now, major on-line travel sites are much more likely to offer Internet-savvy consumers booking options which can go beyond simple transactions such as point-to-point air and hotel reservations. In fact, travel packages are accounting for an increased share of on-line business[4].

1. North American Industry Classification System (NAICS) category 5615 (Travel Arrangements and Reservation Services)
2. NAICS 7211 (Traveller Accommodation: hotels, motor hotels, motels, casino hotels, resorts, and all other traveller accommodations)"
3. Special care should be exercised when using this data to project to the industry level.
4. "Exploding myths: online travel spreads its tentacles", (Bob Mowat, **baxter.net**, September 15, 2003)

The "do-it-yourself" or independent traveller is becoming more prevalent in the Internet age. Consumers can take greater control over their travel plans if they are on-line. Not only is the Internet a useful tool for information gathering, it also allows people to compare prices and options to locate the best deals available.

Such Internet information influences the travel decisions of many Canadians. According to an Ipsos-Reid survey, 35% of on-line Canadians have used the Internet as the primary source of information for planning upcoming travel. As well, a majority said they will use the Internet to research a trip or vacation in the future (87%)[5].

Demand for on-line travel arrangement services has been steadily growing in Canada. Travel arrangement services continue to be one of the most frequently ordered items over the Internet, eclipsed in popularity only by reading materials. In 2003, 22% of households that made on-line purchases reported making travel arrangements over the Internet, up from 18% the year before[6]. As well, referring to the Ipsos-Reid study, 55% of on-line Canadians say that they will likely use the Internet in the future to book travel directly on-line[7].

Nearly two in three Canadian households have at least one member who is a regular Internet user, either at home, work, or another location[8]. Households with children living at home, and with high incomes and levels of education, tend to be the most prevalent Internet users. As well, baby-boomers are reaching an age where they have more time to travel, and more and more of them are using the Internet.

Impact of the Internet on the travel arrangement industry

The increasing popularity of on-line travel arrangement services has brought about a major shift in how travel arrangement providers (tour operators and travel agencies) operate – not least of which is the industry's need to reconcile the on-line business model with the traditional bricks and mortar strategy. Although some consumers are demanding on-line booking capability, others still want to consult face-to-face with an agent, especially once they get to the reservation stage.

On-line agencies have had a huge impact on the travel market. A very popular service is 'dynamic packaging'; where consumers put together their own holiday packages by purchasing their flight, hotel, or car rentals separately.

Whether Canadian travel arrangers meet with their clients face-to-face, on the telephone or over the Internet, many have found themselves an on-line option that works for their firm. For example, some travel service providers use Internet tools such as B2B

5. "More Canadians booking travel on-line: Study", .**globalandmail.com**, August 28, 2003).
6. 2003 Household Internet Use Survey, **Statistics Canada** (The Daily, September 23, 2004).
7. "More Canadians booking travel on-line: Study", (**globalandmail.com**, August 28, 2003).
8. 2003 Household Internet Use Survey, Statistics Canada (The Daily, September 23, 2004).

systems[9] to increase their overall efficiency. Many firms also use the Internet to have access to data provided by other travel-based Web sites. In 2003, the share of tour operators who ran their own company web site increased to 42%, up from 36% in the previous year. In comparison, the share of travel agencies with their own web sites remained steady at 29%.

In 2003, the most common purpose of the company web site was to advertise travel products and services (Table 1). Of businesses with web sites, three-quarters of travel agencies and 84% of tour operators used them for advertising purposes. More travel agencies (60%) than tour operators (49%) used their web sites to enhance customer relations. In 2003, 35% of travel agencies and 34% of tour operators sold goods and services over their own web site.

Table 1: Proportions of companies using web sites for various purposes*

	Travel agencies	Tour operators
Advertise travel products and services	75%	84%
Sell travel goods and services	35%	34%
Enhance customer relations	60%	49%
Other	6%	9%

* Based only on data for firms that do have web sites

Despite their on-line presence, travel agencies generated only 1% of their revenue through their web site. However, this figure may underestimate the true value of Internet sales since Statistics Canada does not survey all on-line travel agencies operating in Canada because some are headquartered and operated out of foreign countries. This makes it problematic to identify this activity within Canada's boundaries.

Tour operators earned about 14% of their revenue through their web sites. The majority of their on-line sales were made to Canadian clients (88%), in contrast to travel agencies which generated most of their on-line revenue (78%) by selling services to foreign clients.

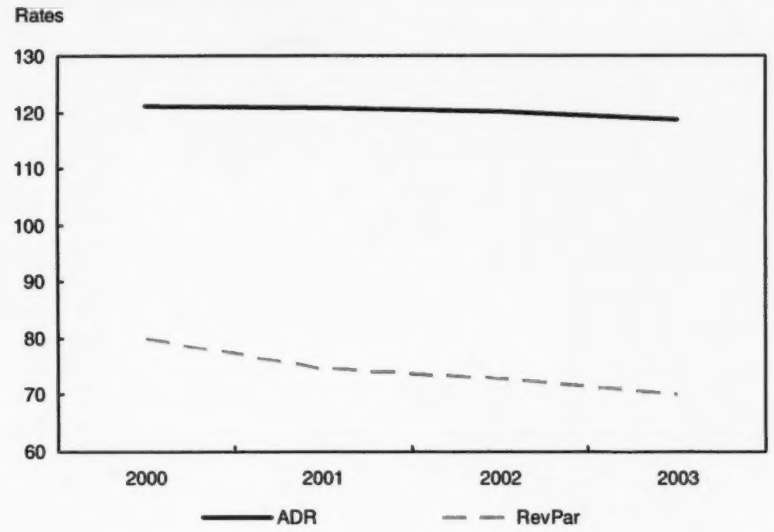
Nearly two-fifths of tour operators felt their businesses benefited from Internet reservations while 45% said they had no effect on their business growth in 2003. In contrast, two in three travel agencies (64%) believed Internet reservations were detrimental to their business. As people become more comfortable making purchases over the Internet they tend to bypass travel agencies, especially those without an online presence.

9. Business to business systems include Internet bookings on an airline Web site.

Impact of the Internet on the traveller accommodation industry

Along with economic conditions and events such as September 11th and SARS, the increased popularity of the Internet indirectly had a negative impact on hotel room rates. Figure 1 shows that hotel room prices dropped from 2000 to 2003 as measured by their average daily rates (ADR). These lower room rates translated into lower revenue per available room (RevPAR) and resulted in lower operating profits. The downward trend in hotel prices can be partly explained by the "merchant model", an approach where hoteliers depend on third-party distributors to unload excess rooms on-line[10]. There are more and more third-party distributors as hotels turn over portions of their room inventory to on-line wholesalers that typically offer lower room rates.

Hotel room prices declining



In periods of sluggish demand some hoteliers turn unsold room inventory to third-party distributors. In most cases, once the inventory is released to these third parties the hotel has little control over room rates which frequently end up lower than those listed by the hoteliers. These room discounts prompt some consumers to expect lower room prices every time they make a reservation, which puts pressure on hotels to decrease the room prices that they still have control over. Hoteliers are in effect competing with third-party distributors that unload excess rooms on-line. A 2002 poll showed that 60% of hoteliers believed that Internet pricing would negatively affect room rates and profit margins[11].

10. Also known as global distribution systems (GDS). GDS is a worldwide reservation system that connects the travel industry to travel agents. With GDS, it is possible to book reservations for travel accommodations, airline tickets, and other travel products. For further information, see E. Brill, Merchant Model or Web Booking Engine?, (Hotel On-line Special Report www.hotel-online.com, December 2003)

11. Given that hotel Internet distribution is an important trend in the industry, many hotel rooms are advertised using on-line hotel consolidators/wholesalers. For hotels that rely on third-party distribution on the Internet, only their discounted rates appear on the web and these discounted rates appear to become the published room rate. Lynds, C. Technology Roundtable' **Hotelier: The Magazine for Hotel Executives**, Kostuch Publications Limited, Toronto, Ontario, January/February 2003.

Use of the Internet as a reservation tool is booming, putting tremendous pressure on non-affiliated hotel and motel operators. These independent operators often lack resources to handle reservations and room rate changes on-line to the extent that affiliated establishments can[12]. Affiliated hotels and motels tend to perform better, at least in part due to having a central reservation system (CRS).[13]

Table 2: Hotels and motels by affiliation, 2003

	Average number of rooms	Average daily rate (ADR)	Revenue per available room (RevPAR)	Occupancy rate
Hotels	**161**	**$ 119**	**$ 70**	**59%**
Affiliated hotels	206	$ 124	$ 74	60%
Non-affiliated hotels	101	$ 104	$ 59	57%
Motels	**57**	**$ 71**	**$ 42**	**59%**
Affiliated motels	81	$ 77	$ 48	63%
Non-affiliated motels	40	$ 63	$ 33	53%

On average, affiliated hotels and affiliated motels had more than twice as many rooms as their non-affiliated counterparts (Table 2). Affiliated accommodation providers were also able to charge higher room rates, earn higher revenues per available room and have higher occupancy rates.

The superior performance of affiliated establishments may be due, in part, to the greater demand that results from being part of a central reservation system. The CRS enables reservations and confirmations to be made through a toll-free owner-operated call centre or a website which is more convenient for travellers. A CRS also helps travellers find a hotel or motel that meets their criteria with respect to location, quality and other characteristics. While much of the superior performance of affiliated establishments may be due to their CRS's, affiliated hotels and motels also likely benefit from brand recognition and other economies of scale and scope including broader marketing and advertising campaigns as well as volume discounts in their own purchases.

12. Deveau, D., 'Get Centered: A Central Reservation System is a Must for Hotels Big and Small, **Hotelier: The Magazine for Hotel Executives**, Kostuch Publications Limited, Toronto, Ontario, January/February 2003.

13. Even if one standardizes for size, by examining only mid-sized firms for example, affiliated hotels and motels tend to perform better than their non-affiliated counterparts.

Part 2: The effect of global conditions on travel industries in 2003

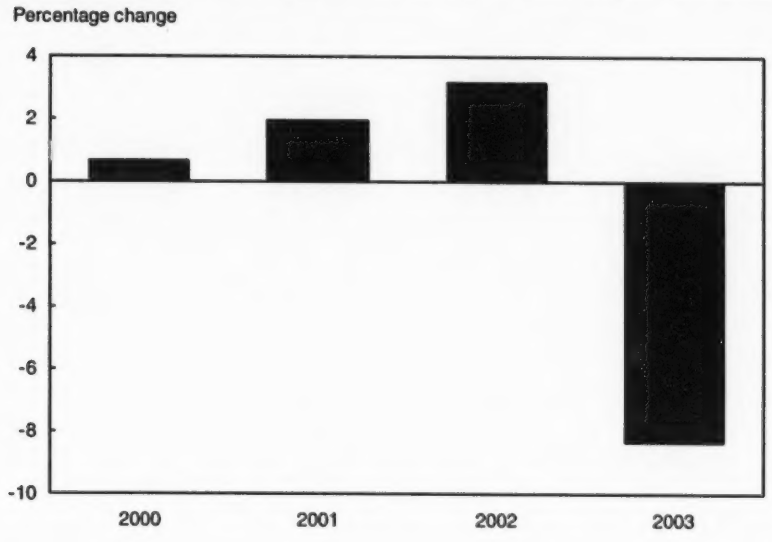
2003 will be remembered as one of the worst years ever for tourism. The Iraq conflict, lingering fears from September 11th, and the unexpected outbreak of SARS had a depressing effect on travel worldwide. Travel declined further in 2003, even after 2001 brought the largest drop in tourism in two decades. Asia and North America in particular contributed to the overall drop in world travel.[14]

A number of other factors made Canada a less desirable tourism destination in 2003. The value of the Canadian dollar rose for the first time in over a decade[15] making it more expensive for some foreigners to visit Canada. Tourism in Canada was further dampened by the West Nile Virus, BSE (Mad Cow Disease), forest fires in British Columbia and a power outage in Ontario. As a result, the number of foreign tourists visiting Canada declined by 13% in 2003.[16]

There was also, for the first time since 1999, a drop in the number of trips made by Canadians within the country[17] (Figure 2). Air transport and accommodation spending were the hardest hit as real spending decreased by 6.2% and 5.2% respectively. Tourism GDP consequently fell by 2.7% in 2003, even though the Canadian economy expanded by 1.7%.[18]

14. Asia experienced a 9.3% drop in foreign visitors due to SARS. North America lost over 15 million tourists between 2001 and 2003 not only from SARS but due to fears from 9/11. **World Tourism Organization, Volume 2, No. 1, January 2004, www.world-tourism.org**
15. The value of Canada's dollar rose from $.64US in 2002 to $.71US in 2003, the first time it exceeded $.70US since 1997 and also the first time the Canadian dollar rose year over year since 1991.
16. Source: **Statistics Canada, International Travel Survey, CANSIM Table 427-0001**
17. Source: **Statistics Canada, Canadian Travel Survey, CANSIM Table 426-0001**
18. Source: **Statistics Canada, National Tourism Indicators CANSIM Table 387-0001**

Decline in trips made by canadian residents within Canada in 2003



Travel arrangements: travel agencies lose while tour operators gain

The travel agency industry in Canada declined in 2003 due to the impact of the Internet, SARS and economic conditions. In terms of revenues, the industry contracted by 1.9% over the previous year. Consequently, the industry's operating profit margin decreased from 6.9% in 2002 to 1.7% in 2003.

The tour operator industry was in a somewhat better position due to the timing of two key events[19]. Although their impacts were felt keenly throughout the year, the outbreak of war in Iraq and SARS occurred during the spring and summer. Since the larger tour operators in Canada tend to specialize in North-South travel, most of which occurs during winter, they had the benefit of a "cooling off" period from the initial onset of these events. As well, the stronger Canadian dollar encouraged travel to southern destinations valued in US dollars. In 2003, the number of trips taken by Canadians overseas increased by 8.4% over the previous year. Much of this growth can be attributed in increases in the number of people travelling to popular sun destinations: Mexico (18.1%), Cuba (49.3%) and the Dominican Republic (29.9%).[20]

19. The tour operator industry, in terms of operating revenues, grew by 6.5% in 2003 over the previous year.

20. Overseas travel includes trips to all foreign destinations except the United States. **Statistics Canada, International Travel Survey, CANSIM Table 427-0001.**

2003 was dismal for traveller accommodation providers

Occupancy rates and operating profit margins dropped in 2003 for the three major traveller accommodation groups (hotels, motels and "other" accommodations) over the previous year (Table 3). "Other" accommodations[21] which mostly include campgrounds and hunting and fishing lodges, was hit the hardest in 2003. This group of establishments had the largest drop in occupancy rates and the lowest operating profit margins. The drop in demand for recreational accommodations can be explained, in part, by unusual weather in parts of Canada during 2003. There were hurricanes in the Atlantic Provinces, wind storms and summer heat waves in Central Canada, drought conditions in the Prairies, and forest fires in British Columbia.

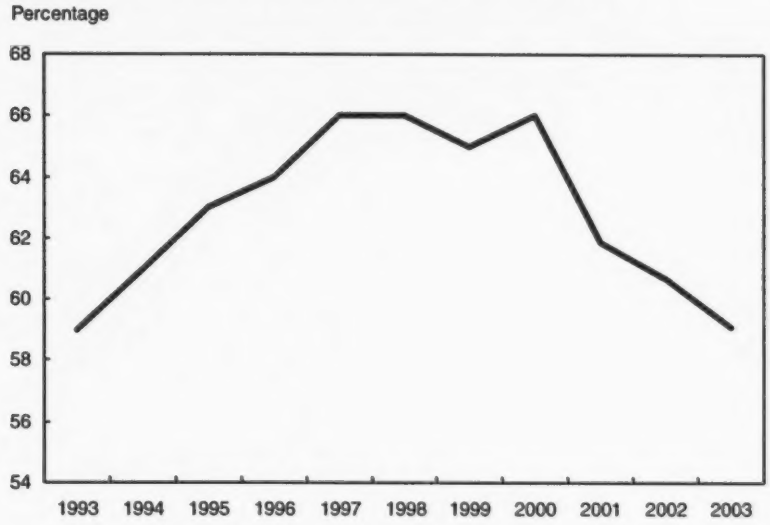
Table 3: Performance decline of traveller accommodation providers in 2003

	Hotels	Motels	Other accommodations
Average number of rooms/guest units available			
2002	161	54	168
2003	161	57	173
Occupancy rate			
2002	61%	60%	69%
2003	59%	59%	65%
Average daily rate(ADR)			
2002	$ 120	$ 72	not applicable
2003	$ 119	$ 71	not applicable
Revenue per available room (RevPAR)			
2002	$ 73	$ 43	not applicable
2003	$ 70	$ 42	not applicable
Operating profit margin			
2002	12.4%	23.3%	14.8%
2003	10.3%	21.2%	6.1%

21. Other accommodations include RV parks and campgrounds (NAICS 721211), recreational and vacation camps (NAICS 721213), outfitters (NAICS 721212), cottages and cabins (NAICS 721192), bed and breakfast (NAICS 721191) and rooming and boarding houses (NAICS 721310).

Hotels experienced a continued decline in demand for rooms as they registered an occupancy rate of 59%. This is the first time the occupancy rate of hotels dipped below 60% since 1993, when the economy was mired in a recession (Figure 3).

Hotels reach the lowest occupancy rate in ten years



Summary

The travel arrangement and travel accommodation industries in Canada face a number of challenges in a rapidly changing and increasingly technological environment. One of the most important recent technology advances, the Internet, may be viewed as an opportunity by some travel service providers while appearing threatening to others. Indeed, a number of travel service providers are increasing their on-line presence, appealing in particular to both time-crunched and Internet-savvy travellers. However, Internet distribution channels and on-line reservation systems appear to indirectly dampen hotel room rates and encourage some travellers to bypass travel agencies entirely.

The traveller accommodations and travel agencies industries were further affected by unfavorable conditions in 2003. Tourism in Canada was significantly impacted by consumer uncertainty related to worldwide events, economic conditions and the weather. However, tour operators in Canada, especially those specializing in trips to Southern destinations, fared better than many other travel industries.